

SERVICE DATE - APRIL 17, 2002

SURFACE TRANSPORTATION BOARD

DECISION

STB Docket No. AB-573X

TRINIDAD RAILWAY, INC.—ABANDONMENT EXEMPTION—
IN LAS ANIMAS COUNTY, CO

IN THE MATTER OF A REQUEST TO SET TERMS AND CONDITIONS

Decided: April 16, 2002

BACKGROUND

On September 1, 2000, Trinidad Railway, Inc. (Trinidad) invoked the class exemption procedures for out-of-service rail lines at 49 CFR 1152.50 to abandon a 28-mile segment of rail line in Las Animas County, CO, between milepost 2.0 at Jansen and the end of the Trinidad line at milepost 30.0.¹ Before that notice went into effect, Rail Ventures, Inc. (Rail Ventures or Petitioner) timely filed a notice of its intent to invoke the Offer of Financial Assistance (OFA) provisions of 49 U.S.C. 10904 in order to acquire the line for continued rail service. That filing, and subsequent extensions, stayed the effective date of the abandonment exemption covered by the notice.² On December 5, 2000, Rail Ventures timely filed its OFA, offering to buy the line for \$2.5 million.

Shortly before that, however, on October 31, 2000, after having received notice of Rail Ventures' forthcoming OFA, Trinidad sold its entire 30-mile line (including the 28-mile segment for which it sought abandonment authority in this proceeding) to Kern Valley Railroad Company (Kern Valley or Respondent), which subsequently invoked the class exemption procedures at 49 CFR 1150.31 to obtain authorization for the purchase. Kern Valley Railroad Company—Acquisition and Operation Exemption—Trinidad Railway, Inc., STB Finance Docket

¹ The procedural history of this and related proceedings is set out more fully and most recently in our January 15, 2002 decision. At the time Trinidad submitted the notice to abandon, the line had not carried any traffic for 4 or more years.

² The Rails to Trails Conservancy (RTC) has requested issuance of a notice of interim trail use (NITU) under the National Trails System Act, 16 U.S.C. 1247(d), in order to negotiate for the acquisition of the right-of-way for rail banking and interim use as a trail. However, because an OFA takes priority over a request for a NITU, RTC's request has been held in abeyance pending the outcome of the OFA process.

No. 33956 (notice served and published Nov. 21, 2000). Kern Valley stated that it did not acquire the line segment to provide rail service, but rather to salvage the rail property once it was abandoned. Kern Valley also acknowledged that the line remained subject to the section 10904 process, a request for issuance of a NITU, and other conditions imposed on the notice of abandonment exemption.

In a decision served December 8, 2000, the Director of the Office of Proceedings found that Rail Ventures was a financially responsible entity and that it intended to restore rail service. The Director also denied a request by Kern Valley to reject the OFA and a request by RTC to dismiss the OFA. In a decision served August 13, 2001, addressing various challenges to the propriety of Kern Valley's acquisition and of Rail Ventures' OFA, we affirmed the Director's decisions approving Kern Valley's purchase and finding Rail Ventures to be financially responsible under section 10904. We stated that either party could ask us to establish the terms and conditions for an OFA purchase of the line, if no agreement on a purchase price could be reached.

The parties were unable to reach an agreement and, on March 18, 2002, Rail Ventures filed a request asking us to set the terms and conditions of sale. Kern Valley replied on March 28, 2002.³

PETITION FOR RECONSIDERATION

In addition to the pending request by Rail Ventures for the Board to set terms and conditions, Kern Valley seeks reconsideration of our December 12, 2001 decision denying its appeal of the Director's decision finding Rail Ventures to be financially responsible and postponing the effective date of the abandonment in order to allow the section 10904 process to proceed. The petition rehashes arguments Kern Valley made in its prior appeal, which we addressed in our December 12 decision denying that appeal. We do not encourage parties to burden the record of proceedings with repetitive arguments and therefore will not address them again. We will deny the petition.

Consistent with our responsibilities under procedures established by section 10904, we will not abort the OFA process at this late stage. The Director's determination of Rail Ventures being financially responsible was supported by the record at the time the finding was made. The initial determination of financial responsibility, made for the limited purpose of postponing the

³ On March 25, 2002, Trinidad also filed a reply to Rail Ventures' request. Trinidad states that information in the request concerning the alleged bankruptcy of the parent company of the only shipper on the line, Lorencito Coal Company, LLC (Lorencito), is erroneous. According to Trinidad, the company filing for bankruptcy was not Lorencito's parent, A.P. Maxwell Development Company, LLC but, rather, AEI Resources Holding, Inc. Rail Ventures, by letter filed on March 26, 2002, admits the error.

abandonment to give an offeror a chance to negotiate to acquire the line, is necessarily based on a preliminary record. This initial determination of an offeror's financial responsibility operates to protect abandoning railroads from suffering delays in consummating abandonments caused by OFAs filed by persons who are manifestly unable to acquire and operate the line.⁴ The postponement of any abandonment, the 30-day period for negotiations, and the subsequent 30-day period for the filing of the request to set terms have already occurred.⁵ The only burden that Kern Valley now faces is the prospect of the actual transfer of the line to Rail Ventures. But the offeror will only be able to obtain the line if it pays Kern Valley the full purchase price we set in this decision. Thus, Kern Valley cannot at this point be adversely affected should Rail Ventures be unwilling or unable to pay the price that we set. Should the OFA sale not be completed, Kern Valley would obtain the result it seeks here—its retention of the line.

One aspect of our prior decision addressing the issue of Rail Ventures's financial responsibility does require some further discussion, however. In upholding the Director's finding of financial responsibility, we noted that Rail Ventures planned to sell the 115-pound rail on the line, replace it with less expensive 90-pound rail, and use the earnings to finance the acquisition. Kern Valley never disputed that a ready market existed for the track, that the proposal was feasible or that 90-pound rail was adequate for anticipated business levels.

However, in the meantime, unit-train coal traffic has returned to the line and Kern Valley, in reply to Rail Ventures' request to set terms and conditions, has justified the consideration of a going concern value for the OFA sale based on providing unit-train service to carry coal. That service, at the volumes we find to be warranted, would require the retention of heavier track on the line, and, as a condition of any sale to Rail Ventures, we are imposing such a requirement. Rail Ventures therefore may be precluded from raising funds by selling the heavier rail.

TERMS AND CONDITIONS

Valuation and Evidentiary Standards

Requests for the Board to set conditions and compensation are governed by the provisions of 49 U.S.C. 10904(d)-(f). Under section 10904(f)(1)(B), we may not set a price that is below the fair market value of the line. Fair market value is defined at 49 CFR 1152.27(h)(6) as the constitutional minimum value, which is the greater of (1) the line's going concern value (GCV) for continued rail use or (2) the net liquidation value (NLV) of the rail properties for their

⁴ This procedure is designed to protect abandoning carriers. Here, however, the abandoning carrier, Trinidad has long since cashed out its investment in the line by selling it to Kern Valley. And, as noted, Kern Valley acquired the line expressly subject to the OFA process.

⁵ In this case, these processes and the resulting postponement of abandonment were protracted by Kern Valley's refusal to comply with discovery.

highest and best nonrail use. See Chicago and North Western Transp. Co.—Abandonment, 363 I.C.C. 956, 958 (1981) (Lake Geneva Line), aff’d sub nom. Chicago and North Western Transp. Co. v. United States, 678 F.2d 665 (7th Cir. 1982). NLV includes the value of the real estate plus the net salvage value of track and materials.

In proceedings to set conditions, the burden of proof as to compensation is on the offeror, as the proponent of the requested relief. Placing the burden of proof on the offeror is particularly appropriate in an OFA context, which involves an involuntary taking of property, because the offeror may withdraw its offer if it considers the price set by the agency to be too high, but the rail carrier must sell its line to the offeror at that price even if it considers the price to be too low. See Lake Geneva Line, 363 I.C.C. at 961. Thus, in areas of disagreement, the offeror must present more detailed evidence or analysis or provide more reliable and verifiable documentation than that which is submitted by the carrier. “Absent probative evidence supporting the offeror’s estimates, the rail carrier’s evidence is accepted.” See Burlington Northern Railroad Company – Abandonment Exemption – in Sedgwick, Harvey and Reno Counties, KS, Docket No. AB-6 (Sub-No. 358X) (ICC served June 30, 1994), at 3, and cases cited therein, and Iowa Terminal R.R. Co. v. ICC, 853 F.2d 965, 969 (D.C. Cir. 1988).

Rail Ventures argues that in this case the Board is precluded from considering the line’s GCV and must set the purchase price at the line’s NLV. Rail Ventures maintains that Lake Geneva Line stands for the proposition that a carrier cannot gain abandonment authority by claiming that a line is an economic burden and then seek a higher going concern valuation at the time of a forced sale under the OFA provisions. Petitioner argues that, instead, the line must be valued on the basis of the facts that existed at the time of the proposed abandonment. Further, Rail Ventures contends that if the line now has a higher GCV, it is only because of the procedural delays that have resulted from Kern Valley’s appeals of Board decisions. Rail Ventures argues that Kern Valley should not be allowed to profit from delaying the OFA process.

In reply, Kern Valley argues that the line’s value should be its worth at the time we set the price. Kern Valley notes that coal movements returned to the line in October 2001 pursuant to a 2-year contract that the shipper (Lorencito) has entered into with the Tennessee Valley Authority, and that the line is now being operated profitably. Accordingly, Kern Valley asserts, we must use the higher of NLV or GCV for the price we set for the line, and it maintains that the GCV is the higher figure in this case.

Usually carriers do not seek to abandon a line that has a GCV that is higher than the NLV. In this case, however, the GCV for the line was affected by the return of a significant amount of traffic during the pendency of this proceeding when Kern Valley began hauling coal from the Lorencito Mine via a contract operator. We cannot ignore any probative evidence relating to valuation, as we are constitutionally mandated to determine the fair market value, which, in an OFA situation, is the higher of the GCV or the NLV. See, e.g., Lake Geneva Line; Fillmore Western Railway Company – Abandonment Exemption – in Fillmore County, NE, STB

Docket No. AB-492 (Sub-No. 2X) (STB served Nov. 1, 2001). Thus, we will consider both the NLV and the GCV.

Net Liquidation Value

Land. Rail Ventures offers no figure for land value, claiming that it has been unable to determine on its own or from its discussions with Kern Valley how much of the property the carrier owns in fee simple. In reply, Kern Valley, the owner of the property, does not include any land value in its NLV estimate. As a result, we will assign no value to land in the NLV.

Track Materials. Rail Ventures submits a recent appraisal performed by Mountain States Contracting (MSC), dated March 24, 2002, of \$2,251,022 for the track materials in the line. As additional support for its estimate, Rail Ventures also submits two appraisals—one from Northwestern Railroad Construction, Inc., dated March 6, 2002, showing an NLV ranging from \$2,200,000 to \$2,500,000, and one from David J. Joseph Company (DJJ), dated March 14, 2002, for \$2,364,500. MSC and DJJ qualified their appraisals in letters to the Board dated March 20, 2002, and March 26, 2002, respectively. Both companies state that they did not realize that their appraisals would be submitted to the Board for the purposes of an OFA, and they add that they did not make any personal inspection of the track materials on the line, but instead relied solely on information furnished by Rail Ventures.

Our review of the appraisals reveals that Rail Ventures apparently used the same quantities of material as an appraisal conducted for Kern Valley by A&K Railroad Materials (A&K) in November 2000, and simply reduced the unit prices to arrive at a lower NLV for the line. We also note that none of the appraisers indicated on what basis the original appraisal submitted by Kern Valley in 2000 was considered to be incorrect or why the lower prices they used were more accurate.

Thus, Rail Ventures has failed to support its offer with sufficient evidence to sustain its burden of proof. All it did was to mail a list of track materials (based on an inspection conducted almost a year and a half ago) to appraisers, who did not inspect the line and who apparently did not know they were being asked to prepare a statement for a section 10904 case. In contrast, A&K based its values on an inspection, and came up with a total of over \$4 million. Rail Ventures' witnesses have given no reason to modify valuations that were based on actual inspections. None of the three statements submitted by Rail Ventures offers any detailed justification for the values it assigned. The estimates are therefore unsupported.

In its reply, Kern Valley estimates the NLV of the line at \$3,830,697. Kern Valley's quantities and quality of track material have been obtained from a recent 2-day inspection of the line by an independent consultant with rail inspection expertise, and its material prices are based

on a verifiable and generally recognized source, the American Metals Market.⁶ Where the offeror has failed to demonstrate that its analysis is supported, we will accept the current owner's figures. In this case, Kern Valley has offered substantial evidence to support these figures. Thus, the record supports a value of \$3,830,697 for the NLV of the line.

Going Concern Value

Overview. GCV is defined as what an entity is worth as an operating business (as opposed to its break-up value) based on its current operations. United States v. Miller, 317 U.S. 369, 375 (1942) (Miller). Although the concept of GCV has been defined and long recognized by the courts, there is no one "prescribed" method for determining GCV. The appropriate methodology varies depending on the facts presented in an individual case. The Board computes GCV by dividing current anticipated operating profit (revenues less costs) by an earnings multiplier (the pre-tax equivalent of the railroad industry cost of capital rate). See Caddo Antoine and Little Missouri Railroad Company-Feeder Line Acquisition-Arkansas Midland Railroad Company Line Between Gordon and Birds Mill, AR, STB Finance Docket No. 32479 (STB served May 5, 2000) (Caddo Antoine).

Use of 2005 Base Year. In the instant proceeding, Kern Valley's witness Gannon developed a GCV of \$5,354,267, based on projected coal tonnage that could move over the rail line during the year 2005, coupled with assumed revenue and cost elements. Kern Valley argues that adopting its 2005 projections as a base year is appropriate because the mine's maximum potential cannot be reached for some years following the resumption of operations in a previously inactive mine. Kern Valley states that it developed its GCV based on our methodology as described in Caddo Antoine, but a GCV based on future expectations does not follow the methodology in that decision, in which the GCV was determined by using the current value of a line, rather than a future value. See Miller at 375. Under that methodology, Mr. Gannon should have developed GCV based on current year 2002 data. As set forth in the Appendix and as further explained below, we find that Kern Valley's year 2002 data, as adjusted, produces a current GCV of approximately \$2.6 million.

Traffic Forecasts. We note that the tonnage forecasts of Kern Valley's witness Shuman, which Mr. Gannon uses in developing GCV, are based on an informational brochure produced by Lorencito in 1998. These figures represent what the coal mine could produce between 1999 and 2011, not how much coal will necessarily be mined, sold, and transported. Although Mr. Gannon treats these figures as what could be sold based on his knowledge of the coal market, these figures are merely production estimates, assuming demand for this coal would actually exist. We further note that the brochure was produced during a time when no coal was being moved over the rail line. Indeed, while the informational brochure projected production of almost 200,000 tons for 1999, 1 million tons for 2000, and 1.2 million tons for 2001, no coal was

⁶ As noted above, Kern Valley offers no valuation for the real estate underlying the line.

actually shipped until October 2001. Moreover, the only committed traffic for 2002 is the Tennessee Valley Authority contract for 20,000 tons per month over the next 2 years (240,000 tons per year)—an amount substantially less than the almost 1.4 million tons used by Mr. Gannon in his development of GCV.⁷ Thus, Kern Valley's tonnage estimates cannot be used and must be restated for the purpose of determining GCV. We recalculated the tonnage of coal to be shipped in 2002, based on Table 1 in the verified statement of Mr. Shuman. Using Shuman's figures for 2002 tonnage and making the necessary adjustment for cleaning factor for underground coal (60%) (see *supra* note 7), we use a figure of 740,000 tons for 2002, well below Kern Valley's projections for 2005. Using this figure, we find the GCV to be \$2,599,495.

Condition Pertaining to Weight of Rail

The record before us indicates that substantial volumes of coal can be expected to move over the line in unit train service—at least 240,000 tons per year for 2 years. Should Rail Ventures purchase the line, any replacement of 115-pound rail with lighter weight rail must first be approved by the Board to ensure that the lighter rail is suitable to handle unit-train coal traffic. A condition to that effect will be imposed on any sale to Rail Ventures.

Summary

We conclude that the NLV for this line is \$3,830,697, based on Kern Valley's estimate, whereas the GCV is \$2,599,495, based on the Board's restatement. Thus, the purchase price is set at the higher (NLV) figure—\$3,830,697. In addition to the conditions specified herein, we will establish our typical OFA terms: (1) payment is to be made by cash or certified check; (2) closing is to occur within 90 days of the service date of this decision; (3) Kern Valley shall convey all property by quitclaim deed; and (4) Kern Valley shall deliver all releases from any mortgage within 90 days of closing. The parties may alter any of these terms by mutual agreement.

Should Rail Ventures elect not to purchase the line under these terms, and should Kern Valley subsequently wish to exercise the abandonment authority that has previously been issued but postponed pending the OFA process, we will require Kern Valley to provide 30 days' advance notice to the Board and to all shippers that have received service from Kern Valley or its operator.

⁷ We also note that the projected volumes of coal to be transported may be overstated, due to the need to clean the coal (washing it to remove dust) and to retain pillars to support the mine. Kern Valley's adjustments for these factors appear to be flawed. A cleaning factor of 60% described as accounting for the loss of volume due to cleaning and the retention of pillars appears to cover only cleaning, and does not account for the losses from retaining pillars.

This action will not significantly affect either the quality of the human environment or the conservation of energy resources.

It is ordered:

1. The purchase price for the line is set at \$3,830,697, and the parties must comply with the terms of sale discussed above.

2. If Rail Ventures purchases the line, such purchase is subject to the condition that the weight of the rail on the line must be a minimum of 115 pounds, unless Rail Ventures can demonstrate to the Board the adequacy of lighter weight rail for handling unit-train coal traffic.

3. To accept the terms and conditions established here, Rail Ventures must notify the Board and Kern Valley in writing, on or before April 29, 2002.

4. If Rail Ventures accepts the terms and conditions established by this decision, Rail Ventures and Kern Valley will be bound by this decision.

5. If Rail Ventures withdraws its offer or does not accept the terms and conditions with a timely written notification, Kern Valley may not seek to consummate any abandonment authority in this proceeding without first providing 30 days' advance notice to the Board and to all shippers that have received service from Kern Valley or its operator.

6. Kern Valley's petition for reconsideration is denied.

7. This decision is effective on the date of service.

By the Board, Chairman Morgan, and Vice Chairman Burkes.

Vernon A. Williams
Secretary

Appendix

GCV Restatement		Kern Valley Base Year 2005	STB Base Year 2002
Tonnages			
1	Underground coal (clean)	380,000	150,000
2	Cleaning Factor	0.6	0.6
3	Underground coal to be shuttled	633,333	250,000
4	Surface Coal	760,000	490,000
5	Total Shuttle Coal	1,393,333	740,000
Revenues			
Shuttle Train Income			
1	Rate per ton	\$1.35	\$1.35
2	Tons	1,393,333	740,000
3	Total shuttle train revenue	\$1,881,000	\$999,000
Unit Train Income			
4	Revenue per train	\$5,300	\$5,300
5	Number of unit trains	87	49
6	Total unit train revenue	\$461,100	\$258,863
Incentive Income			
7	Total unit train tons	1,140,000	640,000
8	Incentive tons benchmark	1,000,000	1,000,000
9	Tons subject to incentive	140,000	0
10	Incentive payment per ton	\$0.55	\$0.55
11	Total incentive payment	\$77,000	\$0
12	Total Revenue	\$2,419,100	\$1,257,863
Operating Costs			
Shuttle Train			
1	CCC Charge per ton	\$0.93	\$0.93
2	Tonnage	1,393,333	740,000
3	Shuttle train charges	\$1,295,800	\$688,200
Unit Train			
4	Charge per unit train	\$3,680	\$3,680
5	Number of unit trains	87	49
6	Unit train charges	\$320,160	\$179,739
7	Total CCR charges	\$1,615,960	\$867,939
GCV			
1	Revenues	\$2,419,100	\$1,257,863
2	Expenses	\$1,615,960	\$867,939
3	Net Revenues	\$803,140	\$389,924
4	Cost of Capital	15%	15%
5	GCV	\$5,354,267	\$2,599,495